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Before the
Federal Communications Commission
Washington, D.C. 20554

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of Implementation of Sections 11 and 13 of the Cable Television Consumer Protection and Competition Act of 1992 Horizontal and Vertical Ownership Limits	MM Docket No. 92-264

COMMENTS OF TIME WARNER ENTERTAINMENT COMPANY, L.P.

February 9, 1993

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Summary

TWE submits that the FCC should promulgate regulations that:

I. THE PUBLIC INTEREST OBJECTIVES OF SECTION II

- ensure that the public interest objectives of § 11 and the overriding policies of the 1992 Cable Act are furthered;
- ensure that the substantial benefits and efficiencies of horizontal and vertical relationships are preserved;

II. PROPOSED RULES REGARDING SUBSCRIBER LIMITS

- impose only national subscriber limits;
- establish a measure of operator size to determine compliance by reference to a percentage which has, (a) as its numerator, the number of cable subscribers served by the cable operator in question, and that has, (b) as its denominator, the sum of (i) the number of all cable subscribers nationally and (ii) the number of subscribers to other multichannel video programming distributors; alternatively, the Commission should adopt a homes passed measure;
- establish a subscriber limit in the range of 30% to 40%;
- adopt attribution criteria that focus on the operator's ability to control a system by virtue of majority ownership;
- grant the Commission sole enforcement authority of subscriber limits exercised at the Commission's own initiative, without certification or reporting requirements;
- adopt a flexible approach to permit waivers and exceptions ensuring that the benefits of horizontal relationships are not jeopardized, creating a waiver that permits expansion into

unserved rural areas and a temporary waiver in other circumstances where commercial exigencies temporarily place an operator over the limits similar to the Commission's existing cross-ownership waiver regulations;

- establish a review of the subscriber limits by the Commission every five years;

III. PROPOSED RULES REGARDING CHANNEL OCCUPANCY LIMITS

- adopt attribution criteria that focus on a cable operator's ability to control a programmer by virtue of majority ownership;
- take account of any broadcast, PEG and leased access channels in the calculation of the channel occupancy limits;
- disregard premium or pay-per-view channels as affiliated programming services in the calculation of channel occupancy limits; alternatively, factor premium and pay-per-view channels into the calculation according to the percentage of subscribers who actually receive them;
- treat multiplexed services (if they are counted at all) as a single service rather than as multiple services;
- apply channel occupancy limits only to national programming services;
- apply channel occupancy limits only to video programmers affiliated with the particular cable operator;
- adopt a channel occupancy limit that permits an operator to carry a number of affiliated services that is high enough to preserve the benefits of vertical integration;
- exempt vertically integrated programming services that have achieved a level of distribution at or above 40% among non-affiliated operators from the channel occupancy limits;

- establish a threshold of 54 activated channels above which the channel occupancy limits no longer apply;
- eliminate the application of channel occupancy limits in communities where effective competition exists;
- grant the Commission the sole authority to enforce the channel occupancy limits on a complaint-only basis, without a certification requirement;
- permit existing vertically integrated relationships which exceed the limit to be grandfathered;

IV. PARTICIPATION IN PROGRAM PRODUCTION

- impose no additional limits on the ability of multichannel distributors to engage in the creation or production of video programming.

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Preliminary Statement

Time Warner Entertainment Company, L.P. ("TWE"), is majority owned and fully managed by Time Warner Inc. ("TWI"), a publicly traded company. TWE consists principally of three unincorporated divisions: Time Warner Cable ("TWC"), which operates cable systems; Home Box Office ("HBO"), which wholly owns two pay-television services (the HBO Service and Cinemax), and is 50% owner of one basic service (Comedy Central); and Warner Bros., which produces and distributes motion pictures and television programs. TWE and TWI also directly and indirectly hold minority interests in various basic cable programming services other than those owned by HBO.

TWE submits these comments in response to Sections V, VI and VII (relating to subscriber limits, channel occupancy limits and participation in program production) of the Commission's Notice of Proposed Rulemaking ("NPRM") adopted December 10, 1992, and released December 28, 1992, regarding its rule-making responsibilities under §§ 11 and 13 of the Cable Television Consumer Protection and Competition Act of 1992 ("1992 Cable Act"), which amend § 613 and add § 617, respectively, to the Communications Act of 1934, 47 U.S.C. § 533, 537. Simultaneously herewith, TWE is submitting separate comments in response to Sections III and IV of the NPRM (relating to sales of cable systems and cross-ownership between cable systems and MMDS or SMATV systems, respectively).

TWE is the plaintiff in a lawsuit pending in Federal District Court in Washington, D.C., in which it takes the position that § 11 and other provisions of the 1992 Cable Act violate its rights under the First Amendment to the United States Constitution. See Time Warner Entertainment Company, L.P. v. FCC, Civil Action No. 92-2494 (D.D.C. filed Nov. 5, 1992). TWE submits these comments without prejudice to its claims and arguments in that lawsuit.

I. THE PUBLIC INTEREST OBJECTIVES OF SECTION 11

As the Commission itself has recognized, § 11 of the 1992 Cable Act requires the Commission to address issues of horizontal concentration and vertical integration in the cable industry that have complex policy ramifications. On the one hand, Congress believed that such concentration and vertical integration should not be permitted to develop further without some check in the form of federal regulation. On the other hand, however, as discussed below, Congress also perceived that horizontal concentration and vertical integration in the cable industry have conferred significant benefits upon consumers, and it directed that the Commission's regulatory initiatives in this area be carefully crafted so as to preserve those benefits. TWE believes that the Commission faces an especially difficult task in carrying out its regulatory charge under § 11(c). For that reason, it comments at some length below on the objectives of that provision and the policy considerations that should guide the Commission in promulgating regulations under it.

Section 11(c)(2) of the 1992 Cable Act directs the Commission to prescribe "reasonable limits" on "the number of cable subscribers a person is authorized to reach through cable systems owned by such person, or in which such person has an attributable interest" and on "the number of channels on a cable system that can be occupied by a video programmer in which a cable operator has an attributable interest". 47 U.S.C. § 533(f)(1)(A), (B). It also directs the Commission to "consider the necessity and appropriateness of imposing limitations on the degree to which multichannel video programming distributors may engage in the creation or production of video programming". Id. § 533(f)(1)(C).

The statute provides a nonexhaustive list of public interest objectives that the Commission is to consider in undertaking these regulatory tasks. The Commission must ensure that cable operators cannot, by virtue of their size or affiliation with particular programming services, "unfairly impede" or "unreasonably restrict" the "flow of video programming" from programmers to consumers or to noncable distributors. Id. § 533(f)(2)(A), (B). The Commission must also ensure, however, that its regulations take account of "efficiencies and other benefits" gained through cable operators' growth and vertical integration and do not "impair the development of diverse and high-quality video programming". Id. § 533(f)(2)(D), (G). The Commission is further directed to "take particular account" of "market structure, ownership patterns, and other relationships" in the cable industry, to ensure that its regulations "reflect the dynamic nature of the communications marketplace" and to avoid regulation that would "bar cable operators from serving previously unserved rural areas". Id. § 533(f)(2)(C), (E), (F).

The Commission's implementation of these public interest objectives must also be guided by the overriding policies of the 1992 Cable Act. These include "promot[ing] the availability to the public of a diversity of views and information through cable television and other video distribution media", "rely[ing] on the marketplace, to the maximum extent feasible, to achieve that availability" and "ensur[ing] that cable operators continue to expand, where economically justified, their capacity and the programs offered over their cable systems". 1992 Cable Act, § 2(b)(1), (2), (3).

In carrying out its charge under § 11(c), the Commission must achieve a delicate balance between, on the one hand, addressing the statutory concern that cable operators' size or vertical integration may "impede" or "restrict" the "flow of video programming" from programmers to consumers and non-cable distributors, and, on the other hand, ensuring that such regulation "rel[ies] on the marketplace, to the maximum extent feasible" and preserves the valuable "efficiencies" and the benefits of "diverse and high-quality video programming" that the growth and vertical integration of cable operators have made possible.

There can be no dispute that consolidation and vertical integration in the cable industry have brought immense benefits to consumers and to industry participants. As the Commission itself found in its 1990 Report to Congress, Competition, Rate Deregulation and the Commission's Policies Relating to the Provision of Cable Television Service, 5 FCC Rcd. 4962 (1990) (hereinafter "1990 Cable Report"):

> "Higher concentration levels in the cable industry have enabled companies to take advantage of valuable economies of scale and foster investment in more and better program sources, which lead to more investment in programming, more original programming and a wealth of new viewing options for consumers." (1990 Cable Report at ¶ 82)

In addition, Congress itself found that "the growth of MSOs in the cable industry has produced some efficiencies in administration, distribution, and procurement of programming", that "programmers' transaction costs also may have been reduced in the absence of the need for negotiation with each of thousands of local cable systems throughout the country" and that "large MSOs" are "able to take risks that a small operator would not" and "can provide a sufficient number of subscribers to encourage new programming entry". House Committee on Energy and Commerce, H.R. Rep. No. 628, 102d Cong., 2d Sess. 43 (1992) ("House Report").

Further, as to vertical integration, the Commission has found that vertical integration between cable operators and cable programmers "produces significant benefits for cable subscribers" by, for example, "providing financial support for faltering program services", thus contribut[ing] to program diversity" (1990 Cable Report ¶¶ 82-83); "promot[ing] the introduction of new services into the increasingly competitive programming services market" (id. ¶ 84); "providing needed capital and a ready subscriber base" for new services and facilitating efficient communications between programmers and program distributors concerning such crucial matters as "viewer taste, reaction to programs and desire for new programs" (id.); reducing "transaction costs normally incurred in acquiring programming" (id.); and "enabl[ing] cable operators to improve the quality of existing program services" (id. ¶ 85). Congress itself recognized these benefits when it directed the Commission to take account of "efficiencies and other benefits" associated with cable operator size and vertical integration and to avoid "limitations which would impair the development of diverse and high-quality video programming". 47 U.S.C. § 533(f)(2)(D), (G).

In addition, Congress assembled substantial quantities of evidence that "vertical relationships strongly promote diversity and make the creation of innovative, and risky programming services possible", and it identified C-SPAN, CNN, Black Entertainment Television, Nickelodeon and the Discovery Channel as "examples of innovative programming services that would not have been feasible without the financial support of cable system operators". House Report at 41, discussing congressional testimony. Similarly, a 1988 study performed by the National Telecommunications and Information Administration ("NTIA") that was considered by Congress in crafting the 1992 Cable Act (see House Report at 41) found that vertical integration confers significant benefits upon consumers by "expand[ing] the supply of cable programming, thus expanding the diversity of viewing choices for subscribers" and by significantly reducing transaction costs. U.S. Dep't of Commerce, Video Program Distribution and Cable Television: Current Policy Issues and Recommendations, NTIA Report 88-233 91 (1988) (hereinafter "1988 NTIA Report").

In crafting regulations that will preserve these benefits of operators' growth and vertical integration while addressing the perceived risks of those industry characteristics, the Commission should be keenly attentive to Congress's policy directive that regulation under the 1992 Cable Act should "rely on the marketplace, to the maximum extent feasible", for it is that marketplace which, in the years preceding the 1992 Cable Act, gave rise to the many benefits noted above.

In addition, in promulgating rules concerning subscriber and channel occupancy limits and considering the issue of cable operators' participation in program production, the Commission must remain keenly aware of the many other regulatory initiatives required by the 1992 Cable Act that the Commission is concurrently undertaking. 1/

As noted above, in directing the Commission to prescribe subscriber and channel occupancy limits and to consider limits on program production, Congress was motivated by a concern that large, vertically integrated cable operators may be able to restrict the flow of video programming to subscribers and to non-cable video distributors. Regulatory initiatives mandated by other sections of the Act take substantial steps toward addressing the congressional concerns articulated in § 11(c).

With respect to Congress's concern that vertical integration may lead cable operators to discriminate against non-affiliated program services or influence affiliated programmers to diminish the availability of their programming to non-cable distributors, see 47 U.S.C. § 533(f)(2)(B), the Commission must remain mindful of its regulatory initiatives under § 19 of the 1992 Cable Act.

1/ TWE notes again that it has challenged the constitutionality of many of those initiatives.

Section 19 requires the Commission, among other things, to promulgate rules that (1) forbid cable operators and vertically integrated programmers "to engage in unfair methods of competition or unfair or deceptive acts or practices" that have the purpose or effect of "hinder[ing] significantly" or "prevent[ing]" a multi-channel video distributor from providing programming to consumers; (2) prevent vertically integrated operators "from unduly or improperly influencing" an affiliated programmer's "decision . . . to sell, or prices, terms, and conditions of sale of" its programming to any unaffiliated multichannel video distributor; (3) prohibit discrimination by a vertically integrated programmer "in the prices, terms and conditions of sale or delivery" of its programming among or between multi-channel video distributors; (4) prohibit "practices, understandings, arrangements, and activities", including certain exclusive contracts, "that prevent a multi-channel video programming distributor from obtaining" programming from a vertically integrated operator. 47 U.S.C. § 548; see also Notice of Proposed Rule Making, in MM Docket No. 92-265, FCC 92-543 (released Dec. 24, 1992). Implementation of the complex array of restraints called for by § 19 will go far toward addressing any concern that vertically integrated firms will in some fashion impede the flow of programming to the public. In addition, the leased access provisions of the

Cable Communications Policy Act of 1984, 47 U.S.C. § 532, which, as amended by the 1992 Cable Act, authorize the Commission to regulate operators' rates for leased access use, see 1992 Cable Act § 9(b), amending 47 U.S.C. § 532(c), will provide additional outlets for programmers who may encounter difficulties in securing distribution by cable operators.

Furthermore, § 12 of the 1992 Cable Act authorizes the Commission to regulate "program carriage agreements and related practices between cable operators or other multichannel video programming distributors and video programming vendors". 47 U.S.C. § 536. In particular, § 12 directs the Commission to promulgate regulations that (1) prevent operators from "requiring a financial interest in a program service as a condition for carriage on one or more of such operator's systems"; (2) prevent operators and others from "coercing a video programming vendor to provide, and from retaliating against such a vendor for failing to provide, exclusive rights against other multichannel programming distributors as a condition of carriage on a system"; and (3) prevent cable operators and others "from engaging in conduct the effect of which is to unreasonably restrain the ability of an unaffiliated video programming vendor to compete fairly by discriminating in video programming distribution on the basis of affiliation or nonaffiliation of vendors in the selection, terms, or conditions for carriage of video programming provided by such vendors". Id. § 536. The Commission's regulatory initiatives under § 12 will also sharply circumscribe any ability of vertically integrated cable operators to impede the flow of programming from programmers to subscribers or to other multichannel video distributors.

In short, through its other regulatory initiatives, the Commission already possesses important tools for fashioning regulations that address congressional concerns about horizontal concentration and vertical integration in the cable industry. Moreover, it must be remembered that those other initiatives address types of behavior that Congress wanted to circumscribe, while § 11(c) is more oriented toward industry structure and therefore has greater potential to inhibit both desirable and undesirable behavior. In promulgating regulations under § 11(c), therefore, the Commission must take care that such regulations, when combined with its other regulatory initiatives, avoid any tendency to impair "the efficiencies and other benefits", including the key benefit of "the development of diverse and high-quality video programming", that are associated with cable operators' growth and vertical integration and that the 1992 Cable Act seeks to preserve. Toward that end, TWE believes that in promulgating regulations under § 11(c), the Commission should, indeed, "rely on the marketplace, to the maximum extent feasible", 1992 Cable Act § 2(b)(2), as Congress has directed.

II. PROPOSED RULES REGARDING SUBSCRIBER LIMITS.

As added by § 11(c) of the 1992 Cable Act, § 613(f)(1)(A) of the Communications Act of 1934, 47 U.S.C. § 533(f)(1)(A), directs the Commission, within one year after October 5, 1992, "to prescribe rules and regulations establishing reasonable limits on the number of cable subscribers a person is authorized to reach through cable systems owned by such person, or in which such person has an attributable interest". The Commission's NPRM requests comment on six principal issues with respect to the subject of subscriber limits: (1) whether the limits to be prescribed by the Commission should be national or regional in scope (NPRM ¶ 35); (2) whether to assess a given cable operator's size in terms of homes passed or under some other measure (NPRM ¶ 36); (3) what percentage should be set as the Commission's limit on the size of a given operator (NPRM ¶ 37); (4) what attribution standards or criteria should be used in determining ownership of cable systems for purposes of applying the prescribed limit (NPRM ¶ 38); (5) what enforcement procedures should be adopted (NPRM ¶ 39); and

(6) whether the Commission should review its prescribed limit periodically and, if so, how often (NPRM ¶ 40).

Briefly summarized, TWE's position on these issues is that (1) only national limits are appropriate; (2) the limits should take into account subscribership achieved by multichannel video distributors other than traditional cable operators, rather than focusing only on cable homes passed; (3) a limit in the range of 30% to 40% is appropriate; (4) attribution criteria should focus on an operator's ability to control the management decisions of a given cable system; (5) enforcement by the Commission on its own initiative is a perfectly adequate, and the most efficient, method of enforcement; and (6) periodic review of the limit is appropriate, but should not occur more frequently than every five years. We discuss each of these issues separately below.

A. Only National Limits Should Be Prescribed.

As a preliminary matter, the Commission asks "whether regional or national subscriber limits, or both, are necessary or appropriate to implement the objectives of the 1992 Cable Act". NPRM ¶ 35. TWE submits that the Commission lacks any authority to promulgate regional limits and that, in any event, regional (or narrower) limits are neither necessary nor appropriate.

In the first place, neither the statutory language nor the legislative history evinces concern with purported "regional" concentration of cable operators. Although Congress set forth its findings concerning the cable industry at some length in § 2 of the Act, nowhere do those findings suggest any concern that cable operators possess undue power at a regional level or have distorted competition regionally or in any particular region. 2/ On the contrary, the legislative findings show concern with issues and objectives that can only be characterized as national in scope. For example, § 2(a)(3) discusses the "substantial increase" in cable penetration nationally and asserts that "the cable television industry has become a dominant nationwide video medium". 1992 Cable Act § 2(a)(3) (emphasis added). Similarly, § 2(a)(4) asserts that "the cable industry has become highly concentrated", id. § 2(a)(4), indicating concern with horizontal concentration in the cable industry as a whole, at the national level.

2/ Obviously, Congress was also concerned with possible competitive dislocations at the local level as well as at the national level. See, e.g., 1992 Cable Act § 2(a)(2) (asserting that "a cable system faces no local competition"). The existence of such local concerns, however, does not warrant injecting into the regulatory process a third, and conceptually distinct, level of regional regulation, as to which the statute provides neither authority nor guidance.

See also S. Rep. No. 92, 102d Cong., 1st Sess. 34 (1991) ("Senate Report") (subscriber limits "address the issue of national concentration in the cable industry") (emphasis added); House Report at 42 (relying upon national statistics and referring to the share "of all U.S. cable subscribers" served by the largest cable operator). Likewise, the statements of policy contained in § 2(b) of the Act make no reference to regional issues, but instead refer to such undeniably national objectives as "promot[ing] the availability to the public of a diversity of views and information through cable television and other video distribution media". Id. § 2(b)(1).

In similar vein, nothing in the language of § 11(c) of the Act expresses any concern with regional issues. Instead, the provision focuses on such decidedly national objectives as securing "the flow of video programming" from programmers to consumers and to other video distributors. 47 U.S.C. § 533(f)(2)(A), (B).

Furthermore, as the Supreme Court has stated, in antitrust analysis "the area of effective competition in the known line of commerce must be charted by careful selection of the market area in which the seller operates, and to which the purchaser can practicably turn for supplies". Tampa Electric Co. v. Nashville Coal Co., 365 U.S. 320, 327 (1961). In the case of cable programming services, this "market area in which the seller operates, and to which the purchaser can practicably turn for supplies", is generally national in scope. 3/ Typically, cable programmers sell, and cable systems and other multichannel video distributors buy, in a national market. The use of satellite technology enables cable programmers to deliver their programming to cable operators and other distributors located throughout the United States. In addition, cable programmers typically secure licenses from the producers of individual programs that permit the programmers to license such programs for exhibition throughout the United States. Because most programming distribution occurs in a geographic market that is national in scope, the imposition of national subscriber limits will best serve the statutory objectives.

Furthermore, neither the statutory language nor the legislative history contains any guidance as to the nature, scope or purpose of any regional subscriber limits. Indeed, neither the statutory language nor the legislative history identifies any regional problems to which such

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3/ There are, of course, some regional networks. Typically, these offer sports programming that is of only regional interest, or obtain only regional rights to sports events as to which the broadcast networks have acquired national rights. Such regional networks are not a major factor in the programming industry, and there is no suggestion in either the language or the history of the statute that they require special regulatory attention.

limits would respond. In promulgating regional subscriber limits, therefore, the Commission would lack any congressionally-prescribed touchstones. Absent some such direction as to proper policy, there is a significant risk that such regulation might cause more dislocations in the distribution of video programming than it would cure.

B. <u>The Subscriber Limits Should Take into Account Subscribership Achieved by Multichannel Video Distributors Other Than Traditional Cable Operators.</u>

The Commission seeks comment on whether the subscriber limits should be implemented based upon an operator's share of cable subscribers or its share of homes passed, and it expresses the view that homes passed "may be a more appropriate and practical measure for this purpose". NPRM ¶ 36. TWE believes that an alternative measure, described below, is more appropriate in view of the statutory objectives.

TWE believes that the subscriber limits should be implemented by measuring the cable operator's share of subscribers who have access to programming either by means of cable or through other multichannel video distributors. Thus, TWE proposes that, in determining compliance with the subscriber limits, the Commission should make its determination by reference to a percentage that has, (a) as its numerator, the number of cable subscribers served by the cable operator in question, and that has, (b) as its denominator, the sum of (i) the number of all cable subscribers nationally and (ii) the number of subscribers to other multichannel video programming distributors.

This approach provides a truer measure of an operator's ability to wield (or attempt to wield) monopsony or other undue market power as against programmers than does any measure based solely on cable subscribership or cable homes passed. Multichannel video distributors other than traditional cable operators provide an alternative distribution outlet to any programmer against which a cable operator may seek to exercise such power. As such alternative distributors proliferate, they will provide increasingly meaningful distribution opportunities to programmers on a national basis. Factoring the subscribers of such distributors into the Commission's analysis is far more consistent with legislative intent than is a measure based solely on cable subscribership or cable homes passed, for any ability of a cable operator to thwart distribution for a particular program service will diminish as the number of subscribers served by alternative distributors increases.

In addition to being a truer measure of the ability of a given operator's ability to effect distortions in programming distribution, the proposed method of calculation avoids unintended consequences that may flow from a